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著者	Allyson MacKenzie, Salvador Andrade Ortiz
著者別名	Allyson MacKenzie, Salvador Andrade Ortiz
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Influence of Japanese Foreign Direct Investment in the State of Guanajuato, Mexico

Allyson MacKenzie, Salvador Andrade Ortiz

Abstract

The objective of this paper is to explore the influence of Japanese Foreign Direct Investment (FDI) in the State of Guanajuato, Mexico. It also aims to provide an overview of the effects of Japanese companies in the way of doing business and the way of living in the state of Guanajuato. These effects are mainly driven by the automotive industry, where Japanese FDI plays an important role. Japanese executives, workers, and their families come along with the FDI inflow becoming an important community, and influencing the cultural and social life in different cities across the state.

Introduction

Foreign direct investment (FDI) is an international capital flow or investment in the form of a controlling ownership in a business in one country by a company based in a different country. Chen (2019) explains that it differs from simple financial or portfolio investment since the foreign companies are directly involved with daily business operations in the host country, forming a relationship over the long-term and includes the transference of resources to acquire lasting management interest in a company. It, therefore, includes the affiliate fusing or becoming a part of the same organizational structure as well as a financial obligation towards the parent company (Hill, 2011; Krugman & Obstfeld, 2006). Ten percent ownership of the voting stock is recognized as the standard minimum stake by the Organization of Economic Co-operation and Development (OECD) for the investing corporation to establish a controlling interest (Chen 2019). Foreign companies do not invest simply by injecting funds but also by bringing knowledge, skills, and technology to the region. For these reasons, the injection of FDI is often in the form of a long-term commitment to a country over several years as opposed to short-term flows or speculative investments that inject and then siphon money out of the host economy creating instability and risk.

Often, when wealthy international companies come to weaker economies, they can either stimulate an existing industry, because of the competition they bring for domestic companies that already exist, or they can create entirely new industries. FDI can also strengthen local economies by creating new jobs and by boosting government tax revenues. Undertaking programs like training staff or building physical infrastructure might only benefit the investing company at first, but as workers develop their skills or learn new ones, they become more educated and valuable. New uses are found for the infrastructure, and as a result, the rest of the economy can benefit (Almfraji & Almsafir, 2013; Munteanu, 2015).

The State of Guanajuato, Mexico

Geography & Climate

Guanajuato, officially the Free and Sovereign State of Guanajuato, with its capital city being the eponymous Guanajuato, is one of Mexico's 32 federal entities. It is a historical region located within a 400 km radius of Mexico City, Guadalajara, and Monterrey in the central area of Mexico. It is part of the macro-region of Bajío (Figure 1) also known as the “Golden Triangle” and is comprised of parts of the states of Guanajuato, Queretaro, Aguascalientes and San Luis Potosi. The Bajío is home to roughly 60% of the nation's population (Guanajuato, 2010; Premium Recruiting for Bajío's Manufacturing, 2016).



Figure 1. The Bajío region in Mexico. From Mexico regions map by P. Fitzgerald, 2008

The state has a temperate climate with an average of 18°C annually with lows reaching 5°C in January and highs of 30°C in May and June. Warm temperatures, together with an average 650mm of annual rainfall in the area, make it an important agricultural region and a top producer in the nation of crops such as broccoli, cauliflower, strawberries and barley (Instituto Nacional de Estadística y Geografía, 2010; Oxford Business Group, 2018:181).

Demography

The state of Guanajuato has a population of close to 6 million people and supplies around 5% of the nation's workforce (Oxford Business Group, 2018), living in 46 municipalities and covering 30,607 km². León is the largest municipality with a population of just over 1.5 million (Instituto Nacional de Estadística y Geografía, 2010), and other large cities include Irapuato, Celaya,

Salamanca, Silao, and San Miguel de Allende, all readily accessible by highway. This proximity allows for a large labor force that is concentrated in a rather small geographic area, with just under 40% of Guanajuato's population living in cities with greater than 100,000 residents (Oxford Business Group, 2018). In addition, the region's proximity to Mexico City, which has over 12 million residents, readily gives those people the option to seek employment and move to The Bajío region to take advantage of the high quality of life the area offers.

Compared to the rapidly aging society of Japan, where approximately 59% of the population is of working age between 15 and 64 years old, 65% of the people living in Guanajuato are of working age. With a median age of 24, even lower than the already low national average of 26, and when contrasted with the current median working age in Japan of over 48 years of age, we readily understand the region's importance as a continuing source of reliable labour for Japanese companies investing in the area (ALFRED, 2019; Japan: Median age of the population from 1950 to 2050, 2019).

Economy and Manufacturing

Historically known for its fertile soil, temperate climate and adequate rainfall, The Bajío has been an important agricultural region since the 19th century. However, in the last decade, it has developed into a mega-cluster of automotive manufacturing for the rapidly growing industry. The website, Strategic Locations for Setting up Manufacturing in Mexico (2019), details that the region has ready access to 80% of the Mexican market share and 70% of Mexico's automotive production within a three-hour radius. Major economic activities identified in this region are: agro-industrial, auto parts/automotive, chemical products, leather shoes, and textiles/clothing/fashion. It is hoped that future growth will include activities such as research services, tourism, medical equipment, pharmaceuticals, and cosmetics (Ministry of Economy, 2017).

This region is also one of the most important logistics centers as a result of its developed transportation infrastructure (Guanajuato, 2010). The Guanajuato Inland Port is a dynamic dry port with the highest growth rate in Mexico and Latin America. It offers 24/7 controlled access and additionally boasts a community services area including, child day-care facilities, a medical centre, a fire station, and sports and recreational facilities to service its employees (Guanajuato Inland Port, 2018; Parque Industrial León-Bajío (n.d.)).

The state's largest and one of its most dynamic economic contributing sectors to its GDP is in manufacturing at greater than 38% of its economic output. Over the past dozen years, industry and manufacturing has grown at a rate of almost 5%. This growth via increased investment in industry has brought with it accompanying benefits such as growth in transport, real estate, and the service sector (Oxford Business Group, 2018). In consequence, one of the reasons why foreign companies have decided to invest in The Bajío region is due to its convenient location, which facilitates the effective export of goods to both the north and the south. From The Bajío, access to the main exits is easily

reached by railway, highways, and seaports, which allow the efficient transportation of goods to almost any part of the world.

Additionally, the country has stable public policies that protect the investor and promote transparency. Qualified labor is another fundamental factor that has strengthened The Bajío's attractiveness for investments. Public and private universities have been important actors in the region's growth. Several campuses and programs have been set up and designed to fill the needs of a growing industrial region. The over 5,000 graduates per year in Guanajuato, places it in the top ten countries for numbers of new engineers (Mexico Will Produce, 2019).

The General Director of JETRO-Mexico, Tadashi Minemura, claims that these favourable conditions have led to increased Japanese investment into the country, especially in the automotive sector (Mexico Now, 2018). The Bajío has over a thousand Japanese companies, mainly located in the cities of Celaya, Irapuato, Salamanca, Leon, Silao, Aguascalientes, Queretaro, and San Luis Potosi.

Japanese FDI in Guanajuato

In the late 1980s and early 1990s, prior to the culmination of the North American Free Trade Agreement (NAFTA), Mexico underwent a profound economic and political reorganization. Changes in legislation in the Law on Foreign Investment were made, and the economy was liberalized. There were reforms in the energy and telecommunications sector, and major state-owned companies privatized, transforming Mexico from a closed economic and political system into an export-oriented industrial economy. This resulted in increased trade between Mexico and the USA (Garriga, 2017; Gomez & Padilla, 2005). By the year 2000, almost 80% of Mexico's trade was with the USA. Around this time, special economic zones in China made their factories very cost-competitive with those in Mexico (Vietor & Veytsman, 2005) and, as a result, Mexico began producing more valuable products, which could remain cost-competitive because of NAFTA.

According to the article *Mexico's Manufacturing Sector Continues to Grow*, (Stratfor Worldview, 2019), Mexico once again became attractive to the manufacturing industry, and several businesses returned after having previously moved operations to China in search of cheaper labor. At present, Mexico's labour costs are almost 20% lower than in China, whereas 20 years ago, they were more than 50% higher. Also, a large pool of qualified workers and incentive schemes that attract FDI is available closer to the United States market. Between 2002 and 2012, automotive exports increased by 152%. The steady pace and consistency with established governmental policies have created an attractive environment for foreign investors and has positioned The Bajío region as a major manufacturing center in North America.

Another growth factor for Japanese investments stated by Mario Fernandez Davalos, of Japanese Practices for KPMG in Mexico, is that "Mexico is a

country with a low-operating cost in regards to automotive manufacturing. In Japan, an employee would cost around \$110 US in terms of manufacturing a car, while in Mexico the cost is \$88 US” (Mexico Will Produce, 2019). To attract foreign investment, in 2006, The Bajío state governments began building infrastructure and training facilities, selling real estate, and providing a wide range of other benefits. As a result, The Bajío region experienced unprecedented economic growth over a ten year period.

The most significant contributing nations to Guanajuato’s accumulated FDI flows between 2000 and 2016 were the United States, 45.1%; Japan, 14.3%; Spain, 11.2%; and Belgium with 8.4%. The nine countries, shown in Table 1, make up 95% of the total accumulated FDI in the period mentioned (Martinez Martinez & Garcia Garnica, 2018).

Table 1. FDI flows in Guanajuato according to country of origin: 2000-2016

<i>Country</i>	<i>Amount(Billion USD)</i>	<i>Participation (%)</i>
The United States	7.77	45.1
Japan	2.46	14.3
Spain	1.93	11.2
Belgium	1.45	8.4
Germany	.79	4.6
Italy	.71	4.1
Canada	.64	3.7
United Kingdom	.31	1.8
Switzerland	.31	1.8
<i>Subtotal</i>	16.37	95
Other countries	.85	5
Total	17.22	100

Source: Martinez Martinez and Garcia Garnica, 2018.

The Bajío region registered an increase of 80.5% of FDI in the 1st trimester of 2017, according to the Ministry of Economy (2017). It has been crowned as one of the leading business sectors in Mexico and is considered, with the arrival of automotive and aerospace foreign investments, the fastest-growing region in Latin America, according to the Ministry of Economy in Mexico (2017). An article from the *El Grande* website (Mexico Will Produce, 2019) outlined that Guanajuato captured most of the FDI in the region with \$424.9 million US, while Queretaro reported \$379.8 million US, an increase of 75.4%, Aguascalientes registered \$341.8 million US, and finally, San Luis Potosi received \$293.47 million US. The state ranking, according to *Doing Business 2016* presented by the World Bank (2020), noted that Aguascalientes and Guanajuato were considered as the best places for opening a business, which is an opportunity that Original Equipment Manufacturers (OEM) have learned

to value. In an August 2019 interview with the online media La Silla Rota (2019), Diego Sinhue Rodríguez Vallejo, Guanajuato State Governor, said that today three of every ten USD invested in Guanajuato comes from Japanese companies, making Japan the main economic partner of the state.

Japanese multinational companies continue to respond with enthusiasm as Nissan invested roughly \$2 billion to build a new automotive plant in Aguascalientes state. Toyota will invest \$1 billion US in a new assembly plant in the state of Guanajuato to produce Tacoma Pickups for the United States and Mexican markets. Honda and Mazda have invested \$120 million and \$500 million, respectively, in their plants in the same state with the Honda plant expecting to create 3,600 direct jobs (Martínez Martínez & García Garnica, 2018). Additionally, Jorge Oliveros Jair Nara, Director of Sustainable Economic Development in Apaseo el Grande, Guanajuato, the municipality where Toyota's new plant was inaugurated, was quoted as saying in the online source *Mexico Will Produce as Many Automobiles as Canada by 2020*, (2019) that "Today Guanajuato has become the most important economic growth platform for doing business in Mexico and is going through an impressive financial moment by having a world-class economic infrastructure."

Japanese companies' influence in the automotive industry in Guanajuato

It is often said that there are *two* Mexicos, the south-southeastern region of the country and the central and north region. The Bajío region is part of the latter, where development can be more tangible. This is in part due to the clusterization process that the states of this region have developed; industrial clusters known as geographic regions where institutions, enterprises, and other related stakeholders interact on a specific productive activity (Porter, 1998).

In The Bajío region there are two well-known industrial clusters, the aerospace cluster in Querétaro State, with Bombardier as the leading Original Equipment Manufacturer (OEM) and the automotive cluster in Guanajuato State with five automotive OEM's. Four out of these five OEM's are Japanese owned, Honda, Mazda, Toyota, and Hino Motors. Additionally, the current Japanese Consul in León, Osamu Houkida, stated in *Milenio Newspaper* that there are 279 Japanese companies operating in Guanajuato (Torres, 2019). If we could outline an area of opportunity for Japanese companies in the region, it would be technology transfer and *know-how*, which could surely generate new tier one, two, or three Mexican suppliers, increasing the wellness of the working Mexican people in the region.

Japanese cultural influence in the State of Guanajuato

The investment of prominent Japanese companies in Guanajuato has influenced the way of doing business and the way of life of the people. In the words of former Japanese Consul in León, Guanajuato, Yasuhisa Suzuki, "Upcoming industries from Japan have increased by 400% the presence of Japanese citizens in Guanajuato. Today more the 2,400 Japanese live in the

state” (Bulman, 2017; Hernandez, 2017). Presently, there are over 3,500 officially recognized full-time Japanese residents in The Bajío region, with the number increasing to over 5,000 if seasonal residents are included (Grajeda, n.d.; Viven en Guanajuato, 2016). Japanese FDI, especially in the automotive industry, drives this immigration. Currently, Salamanca, Celaya, and León have the largest numbers of Japanese living within their communities (Bulman, 2017).

The presence of Japanese firms, especially those in the automotive sector, has brought a new sense to business to the state. Japanese culture, in many ways different from Mexican, has arrived to create synergies and bonds amongst the two countries that will most likely continue to grow and deepen. This interesting wave of FDI coming from Japan to the region has influenced society in different ways. For example, between 2016 and 2018, there were 35 marriages between Japanese and Mexican citizens (Torres, 2019). This will probably represent an increase of young Mexican-Japanese citizens that will continue to increase the Japanese community in the region.

As a result of the large influx of Japanese citizens into Guanajuato, restaurants, hotels, and other service providers have made adjustments in order to cater to the growing number of Japanese customers and are *tropicalizing* their services to satisfy the executives’ and workers’ needs and tastes. For instance, it is not unusual that hotels in Guanajuato include the Japanese channel NHK News among their cable television offerings. A 14-page monthly Japanese language newspaper, *Mexico Shinbun*, began its print in 2015 with an initial distribution of 3,000 to keep the growing number of Japanese living in the area informed on local events, culture, and the arts (Unión Guanajuato, 2015). Also, local restaurants have made an effort to print their menus in Japanese and to include food and drink items on them that are familiar to and suited to Japanese tastes, as well as to play Japanese music for the enjoyment of their guests (Grajeda, n.d.). In the capital city of Queretaro alone, there are over 50 Japanese restaurants.

The most populous city in the state, León, has over 1.5 million inhabitants and over 700 Japanese residents (Bulman, 2017). With this new population, it has begun to undergo other types of changes in its landscape. Corporate branches of the Japanese banks SMBC, Mizuho, and MUFJ operate in León (Hernandez, 2018). In addition, in April 2016, the first Japanese Consulate General opened its doors in León in January 2016 in an effort to promote continuing positive bilateral relations between the two regions (UG’s General Rector, 2016). For example, as seen in Figure 2, welcome signs featuring the Japanese language can be seen on the highways.



Figure 2. Japanese signage on highway, León, GTO. From Mi blog es tu blog by L. Martínez, 2018

Conclusion

It is a fact that Japanese automotive companies have found in Mexico, particularly in the state of Guanajuato, an important partnership. The inflow of FDI in the state coming from Japan has increased year after year and the Japanese influence in the state has become evident. Today in Guanajuato you can find several services by and for Japanese citizens. Even though the global economic scenario remains uncertain for 2020, Japanese OEM's have announced that Guanajuato will continue to be a major link in their Global Value Chains.

During his swearing in as Mexican President on December 1st of 2018 Andres Manuel López Obrador criticized the period of economic liberalization whose breaking point was in 1994 with the beginning of NAFTA. Even though in his first year in office he has maintained a respectful relation with the private sector, uncertainty is palpable. If we add this to the continuous threats of the United States of America's Government to increase tariffs on Mexican imports and the pending ratification of the United States of America, Mexico and Canada Agreement (USMCA) the scene might seem blurry for FDI inflows to Mexico. Nevertheless, the synergies constructed by Japanese Companies in Guanajuato will be difficult to break.

The commitment displayed by global Japanese companies in the state of Guanajuato over at least the last decade, shows the importance the region holds for them. The spillover influences society economically, socially and

culturally, enriching the way of living in many cities of the state. The support of the state government and the welcoming Guanajuato society has created an ideal environment for a sustainable partnership between Japan and Guanajuato.

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